



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

OFFICE OF  
CHIEF COUNSEL

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May 4, 2000

The Honorable John McCain  
United States Senator  
4450 S. Rural Road  
Suite B-130  
Tempe, AZ 85282

Attention: Ms. Geniene Streeter

Dear Senator McCain:

This letter responds to your inquiry dated April 12, 2000, on behalf of your constituent, [REDACTED]. [REDACTED] asked for assistance in estimating his income from mutual funds for purposes of paying estimated tax. As explained below, [REDACTED] does not have to estimate his income from mutual fund distributions to meet his estimated tax obligations.

Taxpayers are required to reasonably estimate their income tax during the year and make estimated tax payments in four installments, due on April 15, June 15, September 15, and January 15 of the following year. The amount of each installment must be at least equal to 25 percent of the taxpayer's required annual payment, or the taxpayer may be subject to a penalty under section 6654 of the Internal Revenue Code (the Code). Because taxpayers are not expected to know exactly what their tax will be for the current year at the time they make their installments of estimated tax, a taxpayer's required annual payment is generally the lesser of: (1) 90 percent of the current year's tax, or (2) 100 percent of the tax shown on the previous year's return (see section 6654(d)(1)).

According to [REDACTED]'s letter, he can't accurately estimate his income from mutual funds prior to distributions. If [REDACTED] tries to pay estimated tax based on 90 percent of his current year tax, he risks underestimating the tax and may be subject to a penalty. A safer alternative for [REDACTED] is to make estimated tax payments based on last year's tax. If he does this, he will satisfy his estimated tax obligations without needing to estimate what his mutual fund distributions will be.

Another alternative that eliminates the need for [REDACTED] to estimate his mutual fund distributions is for him to pay estimated tax using the annualized income method, as described in section 6654(d)(2) of the Code. Where a taxpayer earns income unevenly throughout the year, using the annualized income method may result in lower required installments. If [REDACTED] uses this method, he must attach Form 2210, with necessary calculations, to his tax return. For his convenience, I am enclosing copies of Form 2210 and instructions. I am also enclosing Form 1040-ES, which will assist [REDACTED] in estimating his tax and making estimated tax payments. [REDACTED] has already received Publication 505 from us.

I hope this information is helpful. If you need further assistance, please call me or Nancy Rose (ID #50-06240) at (202) 622-4910.

Sincerely,

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David B. Auclair  
Senior Technician Reviewer, Branch 1  
(Income Tax & Accounting)

Enclosures (3)